FILE COPY

No. 441

# In the Supreme Court of the United States

OCTOBER TERM, 1957

THE LEHIGH COMPANY OF THE STATE OF PENNSYLVANIA

v.

JOSEPH S. MACLAUGHLIN, DIRECTOR OF INTERNAL REVENUE FOR THE FIRST DISTRICT OF PENNSYLVANIA

ON CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE COLLECTOR

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## CITATION

Case:

*MacLaughlin* v. *Alliance Insurance Company of Philadelphia*, No. 548, October term, 1931 ..... 2, 6, 7

Statute:

Revenue Act of 1928, c. 852, 45 Stat. 791, 797, 818, 844, 845—

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# In the Supreme Court of the United States

OCTOBER TERM, 1931

No. 547

THE INSURANCE COMPANY OF THE STATE OF Pennsylvania

*v.*

JOSEPH S. MACLAUGHLIN, COLLECTOR OF INTERNAL Revenue for the First District of Pennsylvania

*ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT*

## BRIEF FOR THE COLLECTOR

### OPINION BELOW

The opinion of the District Court for the Eastern District of Pennsylvania is reported in 49 F. (2d) 361.

### JURISDICTION

The certificate of the Circuit Court of Appeals was filed in this Court December 3, 1931. (Cert. 4.) Jurisdiction is conferred upon this Court by Sec-

tion 239 of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION CERTIFIED

If the basis to be used by an insurance company (other than a life or mutual insurance company) in computing "gain during the taxable year from the sale or other disposition of property," acquired before and disposed of after January 1, 1928, the effective date of the Revenue Act of 1928, be the fair market value of such property as of March 1, 1913, or other basis provided by Section 113 of the Act, is the quoted provision (Section 204 (b) (1), clause (B)) unconstitutional because it taxes capital? (Cert. p. 4.)

STATUTE INVOLVED

(The pertinent provisions of the statute are copied in Appendix A to our Brief, pp. 28–34, in No. 548, *MacLaughlin* v. *Alliance Insurance Company of Philadelphia.*)

STATEMENT

The certificate makes the following statement:

The Insurance Company of the State of Pennsylvania, appellant, plaintiff below, is a stock fire and marine insurance company, incorporated under the laws of the Commonwealth of Pennsylvania.

Joseph S. MacLaughlin, appellee, defendant below, is the Collector of Internal Revenue for the First District of Pennsylvania.

The Revenue Act of 1913 and the subsequent Acts of 1916, 1917, and 1918 taxed all insurance companies in the same manner as corporations generally. Under these Acts gain, which accrued subsequent to March 1, 1913, and was realized during the taxable year from the sale or other disposition of property was taxable as income. Under the Revenue Act of 1921, however, gain by insurance companies (other than mutual) from the sale or other disposition of property was no longer subject to tax nor were such companies permitted to deduct losses sustained in like manner. The Revenue Acts of 1924 and 1926 re-enacted substantially the provisions of the Act of 1921 in this respect. Thus, from January 1, 1921, until January 1, 1928, insurance companies (other than mutual) were not subject to income tax upon gain derived from the sale or other disposition of property.

The Revenue Act of 1928, approved May 29, 1928, became effective as of January 1, 1928, as to all except certain specific provisions not here pertinent, which became effective on the date of its approval.

Section 13 of that Act imposes a tax of 12 per cent upon the net income of corporations generally. Supplement G, which is composed of Sections 201 to 208, inclusive, dealing with insurance companies, provides by Section 204 [c. 852, 45 Stat. 791, 844, 845; U. S. C., Sup. V, Title 26, sec. 2204] as follows:

(a) *Imposition of tax.*—In lieu of the tax imposed by section 13 of this title, there shall be levied, collected, and paid for each taxable year upon the net income of every insurance company (other than a life or mutual insurance company) a tax as follows:

(1) In the case of such a domestic insurance company, 12% of its net income;

* * * * *

(b) *Definition of income, etc.*—In the case of an insurance company subject to the tax imposed by this section—

(1) *Gross Income.*—"Gross income" means the sum of (A) * * *, and (B) gain during the taxable year from the sale or other disposition of property;

* * * * *

(c) *Deductions Allowed.*—In computing the net income of an insurance company subject to the tax imposed by this section there shall be allowed as deductions:

* * * * *

(5) Losses sustained during the taxable year from the sale or other disposition of property;

* * * * *

The foregoing clauses, (b) (1) clause (B) and (c) (5), which provide for the inclusion in the definition of "Gross income" of "gain during the taxable year from the sale or other disposition of property" and that "losses sustained during the taxable year from the sale or other disposition of property" shall be allowed as deductions in com-

puting the net income of such insurance companies, are new.

The Insurance Company of the State of Pennsylvania, appellant, realized gain during the taxable year from the sale or other disposition of property. Appellee assessed and collected a tax thereon from appellant in the sum of $20,933.46 with interest of $885.89, a total of $21,819.35. Such tax was computed upon the theory that the basis to be used in computing gain or loss resulting from the sale or other disposition of property by insurance companies (other than life or mutual insurance companies) on or after January 1, 1928, as applied to property owned on that date, under the provisions of Section 204 of the Revenue Act of 1928 is the cost, the fair market value as of March 1, 1913, or other basis as provided by Section 113 of the said Act.

On August 15, 1930, appellant filed with appellee its Claim for Refund of the said tax with interest so assessed in the sum of $21,819.35. Appellant's Claim for Refund of said tax was disallowed by the Commissioner of Internal Revenue on October 10, 1930. Appellant subsequently instituted the present suit against appellee to recover said sum of $21,819.35 with interest thereon from the dates upon which the same had been paid.

Appellee filed an Affidavit of Defense, raising only questions of law in accordance with the Pennsylvania Practice Act of 1915. The District Court of the United States for the Eastern District of

Pennsylvania (Kirkpatrick, J.) held that, under the provisions of Section 204 of the Revenue Act of 1928 the basis to be used in computing gain from the sale or other disposition of property owned on January 1, 1928, by insurance companies (other than life or mutual insurance companies) is the fair market value as of January 1, 1928, the effective date of the Act, and not the fair market value as of March 1, 1913, or other basis as provided by Section 113 of the Act. The District Court accordingly held that, as so construed, the above provisions of Section 204 of the Revenue Act of 1928 are constitutional. The District Court held the affidavit of defense sufficient and entered judgment for appellee and against appellant.

Appellant subsequently perfected its appeal to the Circuit Court of Appeals for the Third Circuit.

## ARGUMENT

The form of the question is hypothetical, and until the question of statutory construction is determined no constitutional question can arise. It may be that because the question as to the proper construction of the statute is certified by the same court in *MacLaughlin* v. *Alliance Insurance Co.* (No. 548) the hypothetical nature of the question may be ignored. If not, the certificate, of course, must be dismissed.

The question whether the application of the basis prescribed by Section 113 of the Revenue Act of 1928, to the determination of gain upon the sale of

property by a stock fire insurance company renders the taxation of such gains unconstitutional is argued on pp. 20–27 of the Brief for the Collector in *Joseph S. MacLaughlin, Collector of Internal Revenue for the First District of Pennsylvania*, v. *Alliance Insurance Company of Philadelphia*, No. 548, October Term, 1931, now pending upon a certificate from the United States Circuit Court of Appeals for the Third Circuit filed on the same date as the certificate in the instant case.

The facts stated in the instant certificate are substantially the same as the facts stated in case No. 548, and the argument in that case is applicable here.

## CONCLUSION

We respectfully submit that the question certified should be answered in the negative.

THOMAS D. THACHER,
*Solicitor General.*
G. A. YOUNGQUIST,
*Assistant Attorney General.*
SEWALL KEY,
J. LOUIS MONARCH,
*Special Assistants to the Attorney General.*
WILLIAM H. RILEY, JR.,
*Attorney.*

FEBRUARY, 1932.

U. S. GOVERNMENT PRINTING OFFICE: 1932

CLERK'S COPY.

# CERTIFICATE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1931

No. 548

JOSEPH S. MACLAUGHLIN, COLLECTOR OF INTERNAL REVENUE FOR THE FIRST DISTRICT OF PENNSYLVANIA

vs.

ALLIANCE INSURANCE COMPANY OF PHILADELPHIA

ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

FILED DECEMBER 3, 1931

(36362)

# SUPREME COURT OF THE UNITED STATES

## OCTOBER TERM, 1931

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No. 548

JOSEPH S. MACLAUGHLIN, COLLECTOR OF INTERNAL REVENUE FOR THE FIRST DISTRICT OF PENNSYLVANIA

vs.

ALLIANCE INSURANCE COMPANY OF PHILADELPHIA

ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

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1 In United States Circuit Court of Appeals for the Third Circuit

JOSEPH S. MACLAUGHLIN, COLLECTOR OF INTERNAL REVENUE FOR THE First District of Pennsylvania, appellant

*vs.*

ALLIANCE INSURANCE COMPANY OF PHILADELPHIA, APPELLEE

No. 4642. October term, 1931

On appeal from the District Court of the United States for the Eastern District of Pennsylvania

Before BUFFINGTON, WOOLLEY and DAVIS, Circuit Judges

CERTIFICATE TO THE SUPREME COURT

Filed November 23, 1931

The Circuit Court of Appeals for the Third Circuit, in order to be guided to a proper decision of this case, desires the instruction of the Supreme Court, and therefore, under authority of section 239 of the Judicial Code, certifies a question of law arising from the following facts:

*Statement of facts*

The Alliance Insurance Company of Philadelphia, appellee, plaintiff below, is a stock fire and marine insurance company, incorporated under the laws of the Commonwealth of Pennsylvania.

Joseph S. MacLaughlin, appellant, defendant below, is the collector of internal revenue for the first district of Pennsylvania.

2 The revenue act of 1913 and the subsequent acts of 1916, 1917, and 1918 taxed all insurance companies in the same manner as corporations generally. Under these acts gain which accrued subsequent to March 1, 1913, and was realized during the taxable year from the sale or other disposition of property was taxable as income. Under the revenue act of 1921, however, gain by insurance companies (other than mutual) from the sale or other disposition of property was no longer subject to tax nor were such companies permitted to deduct losses sustained in like manner. The revenue acts of 1924 and 1926 reenacted substantially the provisions of the act of 1921 in this respect. Thus from January 1, 1921, until January 1, 1928, insurance companies (other than mutual) were not subject to income tax upon gain derived from the sale or other disposition of property.

The revenue act of 1928, approved May 29, 1928, became effective as of January 1, 1928, as to all except certain specific provisions not here pertinent, which became effective on the date of its approval.

Section 13 of that act imposes a tax of 12% upon the net income of corporations generally. Supplement G, which is composed of sections 201 to 208, inclusive, dealing with insurance companies, provides by section 204 (26 U. S. C. A. sec. 2204) as follows:

"(a) In lieu of the tax imposed by section 13 of this title, there shall be levied, collected, and paid for each taxable year upon the net income of every insurance company (other than a life or mutual insurance company) a tax as follows:

"(1) In the case of such a domestic insurance company 12% of its net income; * * *

"(b) Definition of income, etc. In the case of an insurance company subject to the tax imposed by this section—

"(1) Gross income.—'Gross income' means the sum of (A) * * *, and (B) gain during the taxable year from the sale or other disposition of property.

3 "(c) Deductions allowed.—In computing the net income of an insurance company subject to the tax imposed by this section there shall be allowed as deductions:

* * * * * * *

"(5) Losses sustained during the taxable year from the sale or other disposition of property; * * *"

The foregoing clauses, (b) (1) clause (B) and (c) (5), which provide for the inclusion in the definition of "gross income" of "gain during the taxable year from the sale or other disposition of property" and that "losses sustained during the taxable year from the sale or other disposition of property" shall be allowed as deductions in computing the net income of such insurance companies, are new.

The Alliance Insurance Company of Philadelphia, appellee, realized gain during the taxable year 1928 from the sale or other disposition of property acquired prior to January 1, 1928, and paid a tax thereon. Joseph S. MacLaughlin, appellant, assessed and collected an additional tax from appellee of $4,153.37 with interest of $199.19, a total of $4,352.56, upon additional gain alleged to have been realized by appellee from the sale or other disposition of such property during the taxable year 1928. The additional tax so collected was computed by appellant upon the theory that the basis to be used in computing gain resulting from the sale or other disposition of property by insurance companies (other than life or mutual insurance companies) on or after January 1, 1928, as applied to property acquired prior to that date, under the provisions of section 204 of the revenue act of 1928 is the cost, the fair market value as of March 1, 1913, or other basis as provided by section 113 of the act and not the fair market value as of January 1, 1928, the effective date of the act. The additional tax so assessed represents the excess over the amount of the tax that would have been assessed if the gain had been determined on the basis of the value of the property in question as of January 1, 1928, the basis used by appellee, instead of on the basis provided in section 113 of the act.

4 On August 15, 1930, appellee filed with appellant its claim for refund of the additional tax with interest so assessed in the sum of $4,352.56. Appellee's claim for refund of said tax was disallowed by the Commissioner of Internal Revenue on October 10, 1930. Appellee subsequently instituted the present suit against appellant to recover said sum of $4,352.56 with interest thereon from April 19, 1930, the date appellee paid said additional tax to appellant.

Appellant filed an affidavit of defense, raising only questions of law, in accordance with the Pennsylvania practice act of 1915. The District Court of the United States for the Eastern District of Pennsylvania (Kirkpatrick, J.) held that under the provisions of section 204 of the revenue act of 1928 the basis to be used in computing gain from the sale or other disposition of property owned on January 1, 1928, by insurance companies (other than life or mutual insurance companies) is the fair market value as of January 1, 1928, the effective date of the act, and not the fair market value as of March 1, 1913, or other basis as provided by section 113 of the act. The District Court accordingly held the affidavit of defense insufficient and entered judgment for appellee in the amount claimed with interest.

Appellant subsequently perfected his appeal to the Circuit Court of Appeals for the Third Circuit.

The question of law growing out of the foregoing facts upon which the Circuit Court of Appeals desires instruction by the Supreme Court is:

*Question certified*

Under the revenue act of 1928, is the basis to be used by an insurance company (other than a life or mutual insurance company) in computing "gain during the taxable year from the sale or other disposition of property," acquired before and disposed of after January 1, 1928, its fair market value as of January 1, 1928, the effective date of the act?

JOSEPH BUFFINGTON,
*Circuit Judge.*
VICTOR B. WOOLLEY,
*Circuit Judge.*
J. WARREN DAVIS,
*Circuit Judge.*

[File indorsement omitted.]

5 [Clerk's certificate to foregoing paper omitted in printing.]

6 [Indorsement on cover:] Enter Attorney General. File No. 36,362. U. S. Circuit Court of Appeals, Third Circuit. Term No. 548. Joseph S. MacLaughlin, Collector of Internal Revenue for the First District of Pennsylvania *vs.* Alliance Insurance Company of Philadelphia. Certificate. Filed December 3, 1931. File No. 36,362.

U. S. GOVERNMENT PRINTING OFFICE: 1931